PHILIPPINES ECONOMIC WRAP-UP

AUGUST 05-11, 2000

Summary

New price numbers suggest that inflationary pressures are still well under control, but increases in petroleum costs are starting to have their effect. The new Securities Regulation Code, aimed at curbing insider trading and other abuses, came into effect on August 8, and we report on some of the consequences. Fiscal authorities must have a feeling of deja vu as they try to balance revenues and expenditures in the face of a widening budget gap. Hope springs eternal that shuttered National Steel Corporation can be revived. We also report on signs of recovery in the automotive industry and some developments in the banking industry.

These weekly reviews are available on the Embassy's web site (http://usembassy.state.gov/manila). We provide a longer and more detailed review of the Philippine economy in our May Economic Outlook, which can also be found on our web site.

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FOREX REPORT

The Philippine peso hovered around the P44.80/USD mark as traders watched for signs of interest rate movement in the US and domestically. Movements mostly tracked other regional currencies. From its close of P44.63/USD on July 28, the peso fell to end this week at P44.895/USD.

Exchange Rate Tables

Date	Weighted Average (Pesos/US$)	Closing (Pesos/US$)	Volume (Million US$)
JUL 03	43.436	43.530	98.1
04	43.563	43.535	89.0
05	43.646	43.690	77.5
06	43.851	43.950	123.1
07	43.981	44.030	96.4
JUL 10	44.116	44.305	91.3
11	44.769	44.820	146.3
12	44.866	44.665	162.4
13	44.567	44.705	145.3
14	44.559	44.520	184.0
JUL 17	44.543	44.590	90.0
18	44.622	44.540	106.9
19	44.456	44.510	105.5
20	44.552	44.585	94.5
21	44.510	44.400	121.0
JUL 24	44.529	44.600	108.0
25	44.692	44.755	118.6
26	45.028	45.070	122.5
27	44.989	44.875	125.2
28	44.941	44.860	128.0
JUL 31	44.960	44.835	104.0
AUG 01	44.808	44.860	114.7
02	44.788	44.790	116.0
03	44.763	44.685	134.2

04	44.625	44.630	115.0
AUG 07	44.766	44.845	125.1
08	44.882	44.875	137.1
09	44.819	44.840	102.7
10	44.809	44.870	140.5
11	44.899	44.895	127.6

Source: Bankers Association of the Philippines

CREDIT MARKET REPORT

The Treasury Bureau continues to restrict T-bill and T-bond sales in an effort to moderate interest rate increases. The current debate over this and next year's budget deficit targets (see below) continues to fuel efforts to push rates up. And yet, on a full award of P1 billion, rates on the 91-day T-bill actually sank 0.1 basis points to 8.924%. Longer term paper, however, did not fare so well. The Treasury Bureau rejected all bids for the P1.5 billion worth of 182-day bills being offered; traders said that if all the bills were sold that rates could have risen to 10.25%. As it stands, the 10% rate set at the auction 2 weeks ago (all bids for 182-day bill were rejected on July 31 as well) remains. The Treasury Bureau did allow a modest increase in 364-day bill rates by selling P1 billion worth of the P1.5 billion of bills offered. Rates for the 364-day bills rose 6.6 basis points to 11.242%. P5.345 billion worth of bids for all three tenors were received, a reminder of financial system liquidity. It is worth noting that the Treasury only took in P2 billion of its planned P4 billion total weekly offering, despite pressure to finance the widening deficit.

The August 8 auction of T-bonds tells much the same story. Only P1.825 billion worth of 10-year bonds were sold, despite a planned offering of P3 billion and P3.365 billion in bids. Rates for the 10-year bonds rose 12.5 basis points to 14.625%.

Domestic Interest Rates (in percent)

Treasury Bills

Auction Date	91 days	182 days	364 days
JUL 03	8.890	9.901	10.796
JUL 10	8.890	no sales	no sales
JUL 17	8.890	9.963	10.989
JUL 24	8.919	10.000	11.010
JUL 31	8.925	no sales	11.176
AUG 07	8.924	no sales	11.242

Source: Bureau of the Treasury

Prime Lending Rates of 15 Expanded Commercial Banks

Date of Survey	Average	Range
JUL 05	11.1715	9.50 - 13.500
JUL 12	11.1707	9.50 - 13.500
JUL 20	11.1540	9.50 – 13.500
JUL 27	11.1495	9.50 - 13.500
AUG 02	11.1546	9.50 – 13.500
AUG 10	11.1548	9.50 - 13.500

Sources: Bangko Sentral ng Pilipinas; Press reports

STOCK MARKET REPORT

The 33-share Philippine Stock Index (PHISIX) got a double boost this week from better performance in regional markets and renewed interest in bank and tech stocks. Rumors of a few bank mergers and acquisitions saw a few issues become more active, as did announcements of new tech ventures of a few blue chips. However, trading volumes were at record low levels (on August 7, only P306 million worth of shares were traded -- a seven- year low), partly because of new rules blocking brokers from trading in their own accounts (see below). Poor profit reports also restrained the PHISIX. Overall the PHISIX ended the week at 1474.86, up from its August 4 close of 1451.18.

Philippine Stock Exchange Index (PHISIX) and Value of Shares Traded

Date	PHISIX Close	Value (Million pesos)
JUL 03	1535.65	397
04	1538.88	525
05	1539.92	587
06	1542.41	687
07	1550.60	882
JUL 10	1557.57	765
11	1563.08	738
12	1554.57	902
13	1561.52	1321
14	1553.89	641
JUL 17	1546.60	609
18	1528.85	704
19	1516.99	1,233
20	1489.47	832
21	1479.46	952
JUL 24	1477.80	495
25	1481.60	341
26	1478.33	479
27	1448.90	589
28	1437.08	713
JUL 31	1417.17	1285
AUG 01	1410.33	544
02	1412.77	413
03	1436.06	533
04	1451.18	522
AUG 07	1450.10	306
08	1438.74	450
09	1458.53	649
10	1469.24	788
11	1474.86	490

Source: Philippine Stock Exchange

JULY YEAR-ON-YEAR INFLATION AT 4.2%

The government's National Statistics Office (NSO) reported that July 2000's consumer price index (CPI) increased by 0.5% month-on-month, slowing from 0.7% in June. The CPI increase moderated following seasonally pronounced mid-year hikes in tuition fees and school-related services, products and supplies associated with the June reopening of Philippine schools. However, month-on-month inflation did not slow as much as it did in July 1999 (0.2%) because of larger increases in the food and fuel and utility indices. Two successive typhoons pushed up prices in the heavily-weighted food basket, while fuel and utility rates rose with further hikes in domestic (and international) petroleum prices. As a result, inflation crept up to 4.2% on a year-on-year basis (from June's 3.9% rate).

Economists expect further cost-push pressures as the year progresses, reflecting uncertainties over the direction of world crude prices, foreign exchange jitters, and lingering fiscal difficulties. Two fuel price hikes in July have heightened pressures for increases in transport rates and wages. Manufacturers have hinted that they are finding it more and more difficult to hold off raising prices of basic commodities. Nevertheless, inflation thus far has been lower than expected. Year-on-year inflation averaged 3.6% during the first seven months of the year. Although expected to accelerate in coming months, the government remains confident that the full-year average will remain within the 5-6% range targeted for 2000.

PHILIPPINE CONSUMER PRICE INFLATION
(IN %)

	Year-on-Year	Month-on-Month
Jan 1999	11.6	2.1
Feb	9.9	(0.1)

Mar	8.7	(0.3)
Apr	7.9	(0.1)
May	6.7	0.1
Jun	5.7	0.8
Jul	5.7	0.2
Aug	5.5	0.3
Sep	5.7	0.5
Oct	5.4	0.3
Nov	3.9	0.1
Dec	4.3	0.1
Average		
Jan-Jul 1999	8.0	
Jan-Dec 1999	6.6	
Jan 2000	2.6	0.5
Feb	3.0	0.3
Mar	3.3	0.1
April	3.7	0.2
May	4.1	0.4
Jun	3.9	0.7
Jul	4.2	0.5
Average		
Jan-Jul 2000	3.6	

Source: National Statistics Office

SECURITIES REGULATION CODE -- TRANSITIONAL PAINS

The Securities Regulation Code (SRC), which President Estrada signed into law on July 19, took effect on August 8 (fifteen days after its publication on July 24). In the absence of an official communication from the Securities and Exchange Commission (SEC), the Philippine Stock Exchange (PSE) reminded its members on August 8 that the Code (which is "self-executory") had taken effect. The PSE specifically asked its member-brokers to refrain from dealing for their own accounts ("broker-dealer segregation") to avoid legal complications in the absence of specific SEC guidelines. Market players said that the restriction contributed to low stock trading volumes during the week.

On August 9, the SEC issued a memorandum temporarily upholding all existing rules and regulations, implementing guidelines, circulars, orders and directives of the Commission “which are not inconsistent with the new Code”, until the Commission declares them otherwise. The memorandum also provided that all secondary licenses issued by the Commission (i.e., to act as brokers, dealers, broker-dealers, stock transfer agents, etc.) would remain effective and valid until they expired or were revoked or cancelled by the Commission. SEC officials told the Embassy that the latter provision would, in effect, allow PSE brokers to go on trading for their own accounts. The SEC issued the memorandum to prevent regulatory gaps pending the issuance of implementing rules and regulations for the new Code. A transitory provision in the SRC allows the SEC to defer compliance with certain provisions of the Code (such as the segregation of broker-dealer activities) for up to one year.

There are, however, provisions in the SRC requiring immediate compliance, in particular the reorganization of the PSE board (currently dominated by member-brokers). The SRC directs the existing exchange to reform the board so that non-brokers have a majority. This requires the PSE to increase non-broker membership in its 15-man board from the current three to eight. That SRC provision sought to address strong criticisms magnified by the BW Resources scandal that the PSE was an “old boys’ club” determined to protect, rather than police, its own ranks. At the height of the BW Resources scandal (which caused the SEC to revoke the PSE’s “self-regulatory organization” (SRO) status earlier this year) the SEC had called for a restructuring of the PSE board. The passage of the SRC now gives that SEC instruction the force of law. Impatient with the PSE’s continued foot-dragging, SEC Chair Lilia Bautista said in press interviews that the PSE was already in “technical violation” of the SRC and hinted that her agency was considering imposing sanctions.

SEC CASES MOVE TO COURTS

Also related to the implementation of the new Securities Code, the Securities and Exchange Commission (SEC) endorsed three recent debt payment suspension cases to the Supreme Court for assignment to the regional trial courts (RTC's). The SEC is putting together its records on cases involving intra-corporate disputes, also to be transferred for the courts' disposition. These moves implement a provision in the Securities Regulation Code which transfers to the regular courts the SEC's quasi-judicial powers over intra-corporate disputes and debt suspension and rehabilitation cases filed after June 30, 2000. Earlier this year, the SEC (with the help of foreign donors such as USAID) released more detailed and systematic guidelines and procedures for debt recovery. SEC officials told the Embassy that they provided the Supreme Court a copy of the said guidelines, but had no indication as yet on whether they would be adopted. SEC officials also said that the Supreme Court intended to designate specific trial courts which would hear intra-corporate and debt suspension cases. Pending the issuance of clearer procedures, however, the transfer of the SEC's quasi-judicial functions to the courts has raised concerns over potential delays arising from an overburdened and capricious court system.

THE FISCAL CROSSROAD

The government is once again at that all too-familiar crossroad: should it widen its fiscal deficit or further squeeze expenditures? Department of Finance Secretary Jose Pardo hinted in press interviews that the national government's P62.5 billion fiscal deficit target would have to be widened (by up to P20 billion) in the wake of internal revenue and privatization collection shortfalls. On the other hand, Budget Secretary Benjamin Diokno has said that the government is bent on keeping the deficit within the targeted ceiling. If revenues continue to fall short, that means cuts to an already tight spending plan -– with the axe likely to fall heaviest on "non-discretionary" items such as maintenance and capital outlays.

This year's fiscal dilemma will put the government's more expansionary 2001 budget proposal under even closer scrutiny. The national government has proposed a P725 billion budget authorization for 2001 (11.6% more than in 2000). It also envisions a wider P85 billion deficit to fast-track foreign-assisted projects and stimulate economic activity. Members of the Senate finance committee hinted that, like 2000, another prolonged congressional debate was possible. The 2000 budget was signed by President Estrada in February, a month and a half into the fiscal year.

BANKING NOTES

Bank Reserves: Recently-issued BSP Circular 254 shifts to a "lagged system" of computing reserve requirements on deposit and deposit-substitute liabilities. Effective October, banks' and quasi-banks' reserve requirements for a current reference week will be computed based on the corresponding levels of deposit/deposit-substitute liabilities of the prior week. The lagged system of providing for required reserves eliminates the guesswork involved in the current system, under which banks and quasi-banks have tended to regularly "overprovide" reserves relative to their estimated, daily deposit levels. By freeing up excess reserve provisions, BSP officials hope the measure will lower intermediation costs and lending rates.

PNB: The recently privatized Philippine National Bank (PNB) posted a net loss of P1.4 billion during the first half of 2000. Saddled with a non-performing loan ratio of over 35%, officials attributed the bank's first semester loss to lower interest income and higher provisioning for bad debts. Last month, stockholders approved a stock rights offering (initially targeted at P10 billion) to help get the bank back on more solid financial footing and to put it in compliance with Bangko Sentral capital adequacy requirements.

ExportBank and PBCom: Export and Industry Bank (ExportBank), which ranks among the country's smallest commercial banks is reportedly "exchanging information" with a foreign bank for a possible buy-in into the local banking institution. The Philippine Exporters Confederation (Philexport) currently holds a 60% stake in ExportBank and the Lippo group an estimated 30%. If talks prosper, the buy-in will mean an overall dilution of existing stockholders. Meanwhile, Philippine Bank of Communications (PBCom) -– which ranks among the largest

20 banks in the country by assets -- is going it alone for now after a number of exploratory merger talks fell through. The bank's stockholders recently voted to increase authorized capital stock in preparation for a planned P2-3 billion stock rights offering in September. These developments reflect growing pressures for smaller commercial banks to try and stay in step with the larger institutions emerging from the mergers and acquisitions sweeping through the banking industry.

RECEIVERSHIP COMMITTEE PROPOSES NSC REVIVAL

A receivership committee tasked to map out a bailout plan for National Steel Corporation (NSC), the only integrated steel mill in the country, asserted that the NSC is "not a terminal case despite being comatose" for nine months. NSC closed down in November 1999 due to steadily plunging sales and soaring interest rate expenses resulting from the Asian financial crisis. Its recovery would require the support of the government to curb cheap imports through the imposition of anti-dumping duties. In its appeal to revive the company, the committee has urged the government to act quickly on NSC's dumping cases against some 30 foreign suppliers of hot rolled coils, billets and tinplates. Another committee proposal is to exempt the company from a WTO policy which mandates that only companies which account for 50% of domestic output can file a petition for anti-dumping and seek compensation for its injuries. The committee argues that the revival of a large and integrated domestic supplier like NSC (with 2,000 employees) would complement the government's policy of promoting and securing competition to bring down prices and stimulate demand.

A recent audit by creditor banks shows that almost all of NSC's operations, except for its hot mill, could be run profitably. That assumes NSC obtains full backing from the government in terms of tariff protection and stricter implementation of anti-dumping measures. The receivership committee is leaning toward a) takeover of NSC by its 14 creditor banks (led by Philippine National Bank), b) infusion of $30 million in new capital to restart operations, c) installation of a new management team, and d) restructuring of NSC's P16 billion (about $360 million) debt. Trade and Industry Secretary Mar

Roxas has expressed disappointment that after conducting negotiations with half a dozen companies, so far, offers received merely involved tolling arrangements. According to the receivership committee, the ideal buyer of NSC would have at least $130 million in cash to restart the steel facility, about $600 million to rehabilitate the company, and be well connected to suppliers of steel slabs, NSC’s basic input. The government is willing to dilute its 12.5% stake in NSC in favor of a new investor with long-term plans for the company.

AUTO SALES RECOVERY CONTINUES

The automotive industry continues to show signs of recovery with total sales for the first seven months climbing 19.7% to 49,303 units (from 41,194 units a year ago), the Chamber of Automotive Manufacturers of the Philippines, Inc. (CAMPI) reported. Sales of light commercial vehicles (LCV), which accounted for 63% of total sales, grew 23%, while passenger car sales (37% of total sales) rose 13% year-on-year.

After a 7% year-on-year decline in industry sales to 74,414 units in 1999, assemblers are once again optimistic that the automotive sector would be able to hit an earlier 13% growth target of 84,000 units by year end. A CAMPI official noted that easier access to financing and a renewed “appetite” for improved models of "Asian Utility Vehicles" and the broad range of newly launched economical, compact cars fueled robust sales. However, a new round of price increases implemented in August by most assemblers (to cover the impact of the weakened peso and higher production costs) raises doubts that the automotive industry would be able to sustain the pace of recovery.